

CALIFORNIA INFRASTRUCTURE AND ECONOMIC DEVELOPMENT BANK

STAFF REPORT

ISSUE

At its September 29, 2009 meeting, the I-Bank Board received a report describing activities that have taken place between 2003 and 2009 by the Imperial Irrigation District (IID) to meet the conditions established in the Preliminary Loan Guarantee Commitment approved by the Board on June 23, 2003 ("Commitment").

At that meeting, the Board requested continued monthly updates on the status and progress of IID's activities in relation to the Commitment and a report on I-Bank staff's review of IID's application for a Final Loan Guarantee.

As previously reported, in a letter to the I-Bank dated August 29, 2009, bond counsel for IID asserted that one of the Commitment conditions should be deemed "inapplicable", and requested confirmation that the statutory condition to the I-Bank's obligation to seek additional funding for the IID guarantee trust account could be met subsequent to the issuance of the I-Bank's Final Loan Guarantee. On September 14, 2009, the I-Bank received IID's formal application for the issuance of a Final Loan Guarantee which was supplemented by IID on October 1, 2009. The IID's formal application incorporated the assertions of the August 29, 2009 letter.

I-Bank staff has reviewed IID's application to determine whether IID has met the conditions set forth in the Preliminary Loan Guarantee Commitment, and whether its requests to have a condition deemed "inapplicable" is advisable.

CURRENT STATUS

I-Bank staff has performed a review of the IID formal application and sent a letter to IID indicating that the application is considered substantially complete, and requesting additional information or clarification of several items. IID has responded to this request, and provided some but not all of the additional information and clarification requested. IID and I-Bank staff will be meeting in the near future to discuss the unresolved issues. At this point, three key unresolved policy issues are:

- **Loan Guarantee Amount (Commitment Condition #4):** IID's application states that the "aggregate amount of the loan guarantee shall not exceed principal amount of Bonds, which IID expects to issue in two or more series, that results in \$150 million of net project costs." By the terms of the Commitment and the Criteria, Priorities and Guidelines (Criteria) adopted by the I-Bank Board, the maximum loan guarantee amount cannot exceed (a) \$20 million and interest earnings thereon and (b) an amount allowed by the "reserve account requirement." Inasmuch as the "reserve account requirement" has not been established by the California Legislature, the current loan guarantee maximum is limited to the approximately \$24 million currently held in the IID Guarantee Trust Account

and interest earnings thereon. I-Bank staff will require that all bond documents clearly reflect the current scope of the guarantee and express that though the I-Bank's Executive Director would be statutorily obligated to seek additional funding when and if the Legislature establishes a "reserve account requirement", no such requirement has yet been established, that no assurances can be made that the "reserve account requirement" will be established, and that no assurances can be made that any request by the I-Bank Executive Director would be successful in obtaining additional funding.

- Reimbursement and Indemnification Agreement (Commitment Condition #14). IID asserts that the reimbursement condition is "inapplicable." I-Bank staff is unaware of any agreement by the I-Bank Board that, should the guarantee be drawn upon, the I-Bank would not have rights to reimbursement, as is commonly provided to guarantors. I-Bank will require all relevant bond documents as well as the final loan guarantee to incorporate appropriate reimbursement provisions.
- Draw Event. IID and I-Bank staff agree that the guarantee is for the purpose of addressing certain financial risks to IID and to enable IID to issue sufficient revenue bonds to finance a water supply project that meets the requirements of the Criteria. (Criteria, Section B). IID proposes a guarantee that may be drawn upon in the event of any non-consensual termination of the QSA and related documents. I-Bank staff believe that the Criteria were based on an understanding of the I-Bank Board that there were two types of early termination which would give rise to the draw on the guarantee. Those are the events of early termination set forth in the QSA and related agreements, and which either result from costs of environmental mitigation which exceed 2003 cost estimates or the San Diego County Water Agency's ability to terminate its water transfer agreement with IID in 2037 after giving notice of its intention to do so in 2017.

In addition, in reviewing the bond disclosure document submitted by IID as part of its application, I-Bank staff has identified a number of different pending litigation matters that may delay the issuance of the IID bonds to which the I-Bank guarantee would apply. I-Bank will work with IID to determine what type of "conditional" guarantee agreement it is proposing in light of the likely delay in bond issuance as a result of this pending litigation.

Finally, I-Bank has engaged special counsel to advise and assist the I-Bank with the drafting of the final loan guarantee.

Bank staff will keep the I-Bank Board apprised of any significant developments